



# BOQ

## FY16 RESULTS PRESENTATION

### 6 OCTOBER 2016

FOR THE YEAR ENDED 31 AUGUST 2016



## RESULTS OVERVIEW

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JON SUTTON  
Managing Director & CEO

## FINANCIAL DETAIL

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ANTHONY ROSE  
Chief Financial Officer

## SUMMARY & OUTLOOK

JON SUTTON  
Managing Director & CEO

# STRATEGY REMAINS UNCHANGED

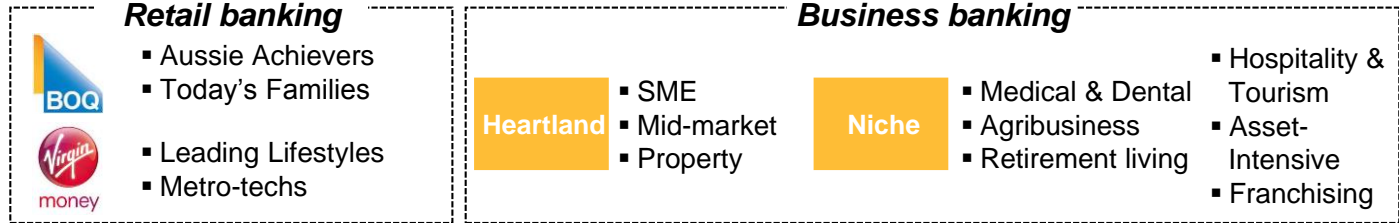
Vision ...

Our dream is to create AUSTRALIA'S MOST LOVED BANK

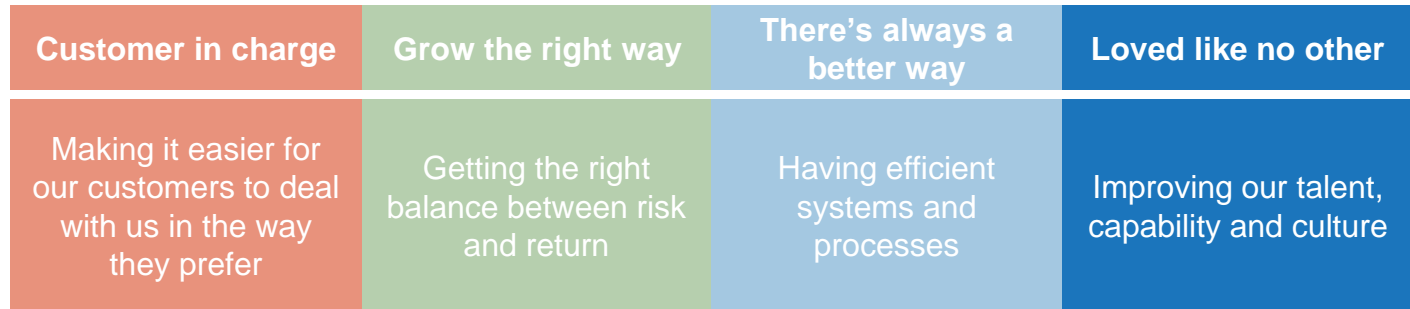
Strategy ...

Focus on niche segments that value a more intimate customer relationship

Target segments ...



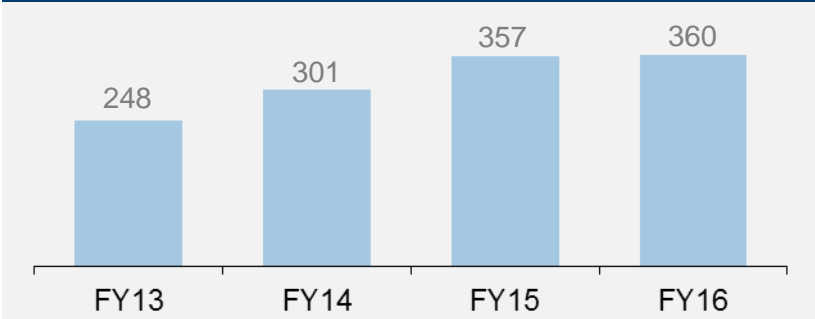
Strategic pillars ...



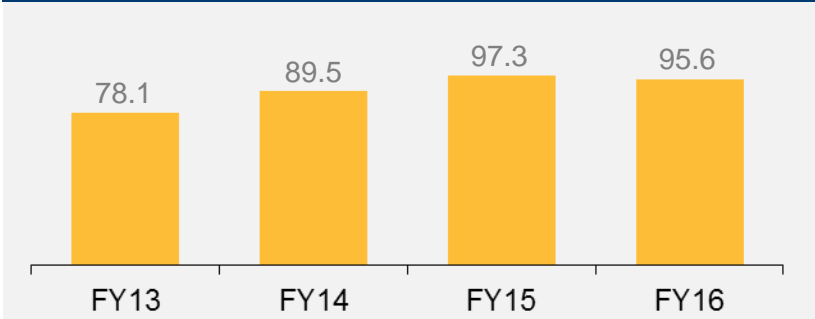
- 1 Increased profit in a changing operating environment
- 2 Niche specialist businesses delivering strong results
- 3 Strong asset quality
- 4 Significant focus on productivity and deposits
- 5 Progressing well with execution of strategy

# KEY ELEMENTS OF THE RESULT

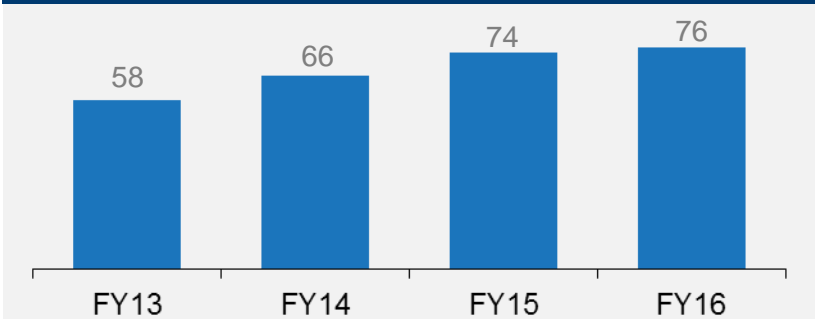
## CASH EARNINGS AFTER TAX (\$M)



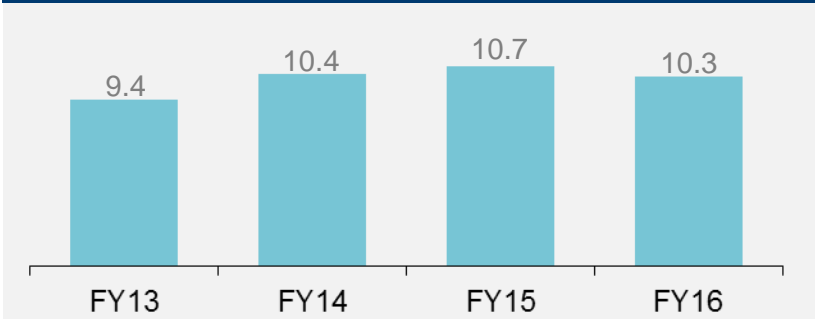
## EARNINGS PER SHARE (CENTS)



## DIVIDENDS PER SHARE (CENTS)

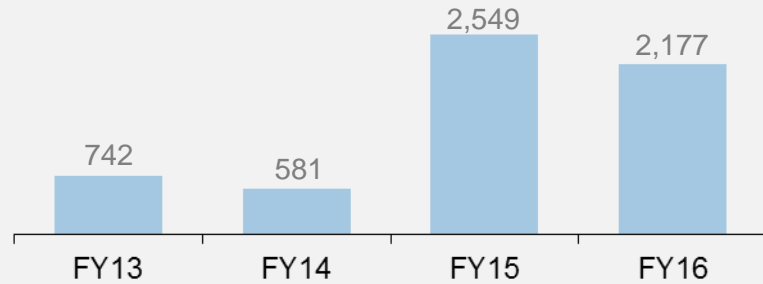


## RETURN ON EQUITY (%)

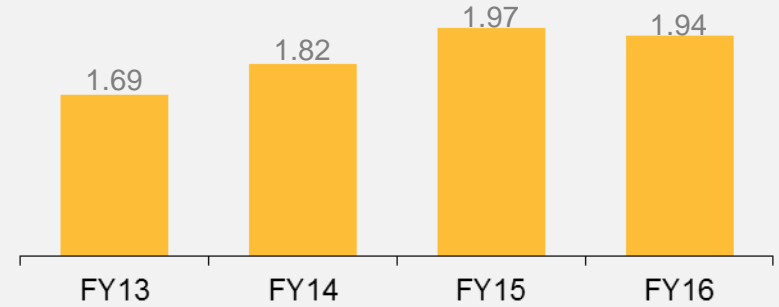


# DRIVERS OF THE RESULT

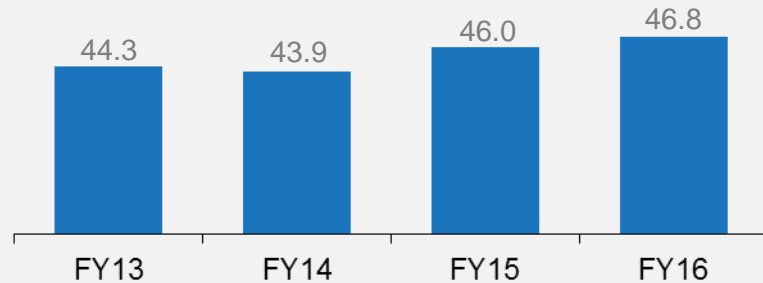
## LENDING GROWTH (\$M)<sup>(1)</sup>



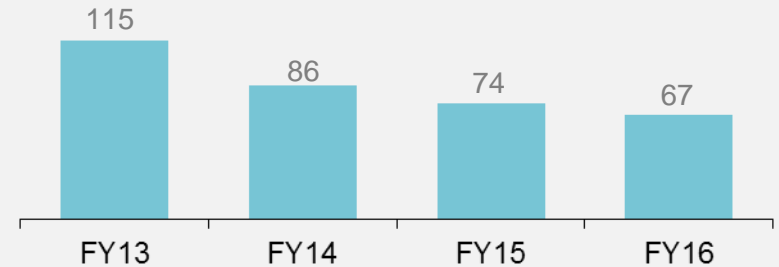
## NET INTEREST MARGIN (%)



## COST TO INCOME RATIO (%)



## LOAN IMPAIRMENT EXPENSE (\$M)



(1) FY14 excludes the addition of the BOQ Specialist portfolio

## BOQ SPECIALIST

- Commercial loan book growth 13%
  - High margin business
  - Benign loss experience continues
- Housing loan book growth of \$1.5bn
  - High quality residential loan portfolio



## BUSINESS BANKING SEGMENT GROWTH

- Bankers and credit teams aligned to target segments
- Growing above system – total niche business segment growth of \$500m in FY16 or 16%

## BOQ FINANCE

- Portfolio growth of 3% in a flat market
- Focus on higher margin business
- Impairment expense within expected range



## VIRGIN MONEY

- Mortgage product launched in May with ~800 brokers now accredited
- Next evolution to be deposit products
- Growth in credit card book & insurance products demonstrate power of the brand

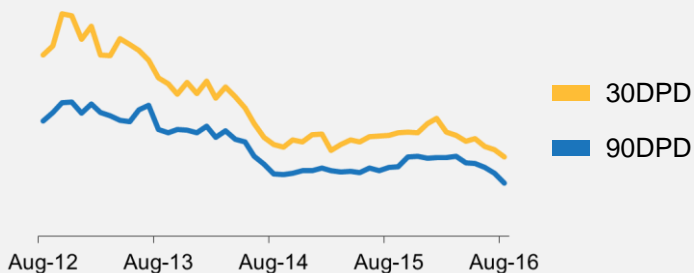


# IMPROVING ASSET QUALITY HAS BUILT RESILIENCE

## SUMMARY

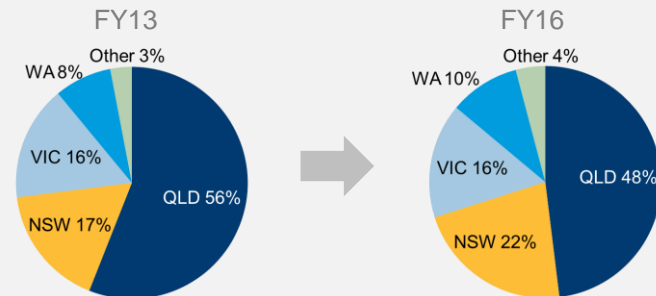
- The business is now much better placed to operate sustainably through the inevitable economic cycles
- 65% of housing loans written from FY13 onwards, under more conservative risk settings
- Limited exposure to apartment development hotspots
- Sound risk management has meant no significant impact to overall portfolio from mining and regional QLD downturn

## COMMERCIAL LOAN ARREARS<sup>(1)</sup>

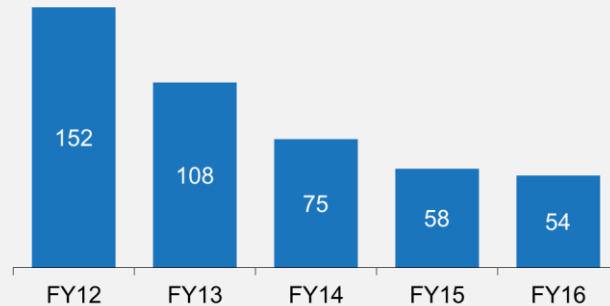


(1) Excludes BOQ Specialist  
(2) Includes BOQ Specialist from FY14

## GEOGRAPHIC DIVERSITY – GROSS LOANS



## IMPAIRED ASSETS % OF GROSS LOANS (bps)<sup>(2)</sup>



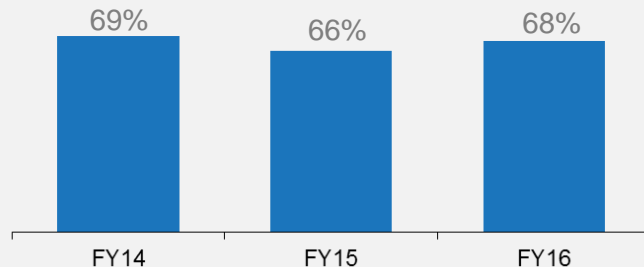


# ADAPTING FOCUS TO FIT THE OPERATING ENVIRONMENT

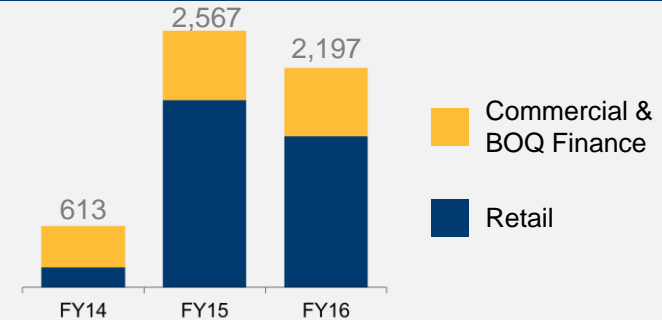
## SUMMARY

- Revenue under pressure across the sector – lower credit growth and ‘lower for longer’ interest rate environment
- Net Interest Margin impacted by market dynamics post-May RBA cut: lower yield curve and higher TD spreads
- Prioritised margin over growth in 2H16
- Retail network increased emphasis on deposit growth in 2H16

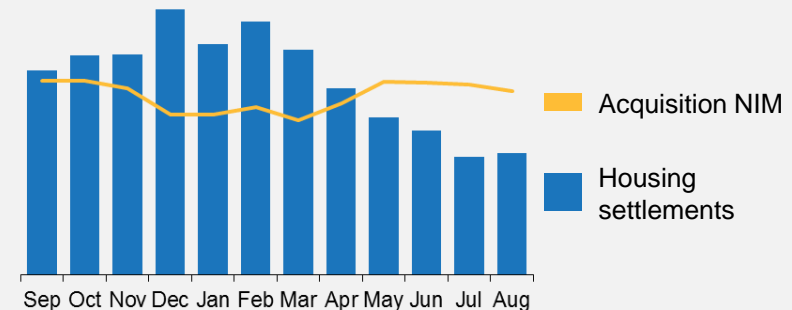
## DEPOSITS TO LOAN RATIO



## ASSET GROWTH COMPOSITION<sup>(1)</sup>



## HOUSING SETTLEMENTS VS ACQUISITION NIM

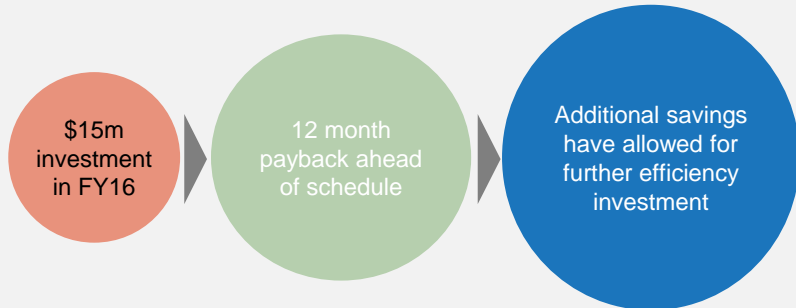


(1) Excludes Consumer lending

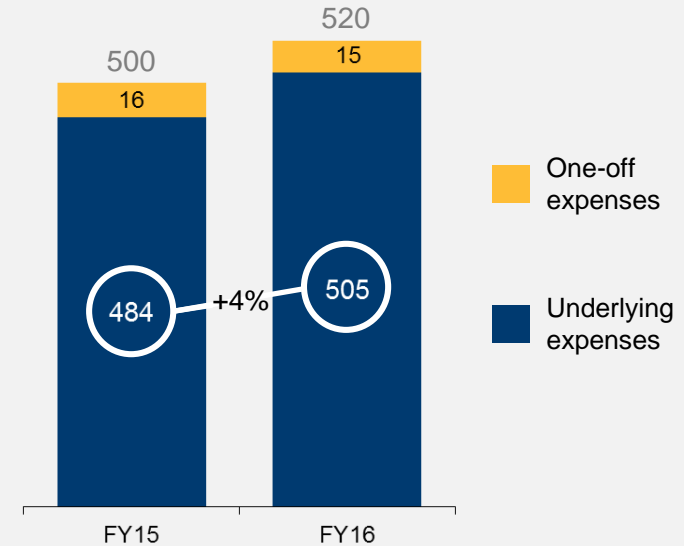
## SUMMARY

- Elevated importance and focus on productivity and efficiency programs
- Additional efficiency initiatives underway within current expense profile
- 4% underlying expense growth in FY16; targeting 1% underlying growth in FY17














## \$15M INVESTMENT PAYBACK ON TRACK



## TIGHT UNDERLYING EXPENSE MANAGEMENT



# FY16 SCORECARD: STRATEGIC PRIORITIES

Strategic pillar	FY16 priorities	FY16 progress
<p><b>Customer in charge</b></p>	<ol style="list-style-type: none"> <li>1. Expand BOQ accredited brokers to 4,000</li> <li>2. Roll out Virgin Money mortgage product</li> <li>3. Digital enablement</li> <li>4. Ongoing branch network optimisation</li> </ol>	<p>        </p>
<p><b>Grow the right way</b></p>	<ol style="list-style-type: none"> <li>1. Continue to increase customer deposits</li> <li>2. Maintain discipline in pricing and credit quality</li> <li>3. Grow specialist niches</li> </ol>	<p>      </p>
<p><b>There's always a better way</b></p>	<ol style="list-style-type: none"> <li>1. Roll out new Lending origination system</li> <li>2. Utilising data analytics</li> <li>3. Continue to invest in risk foundations</li> </ol>	<p>      </p>
<p><b>Loved like no other</b></p>	<ol style="list-style-type: none"> <li>1. Instil sales and service culture</li> <li>2. Invest in leadership and talent</li> <li>3. Build diversity</li> </ol>	<p>      </p>

Legend:  Achieved  Achieved & ongoing  In progress



# FINANCIAL OVERVIEW

ANTHONY ROSE  
Chief Financial Officer



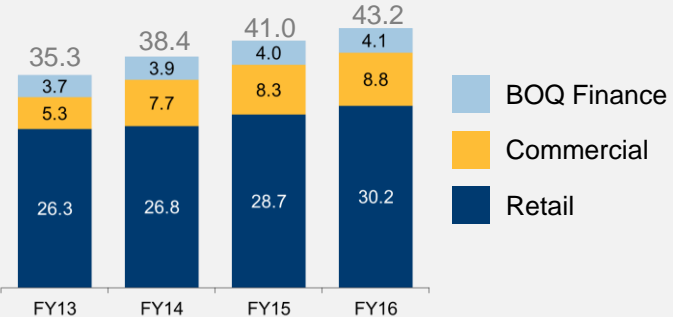
	FY16	FY16 v FY15
Net interest income	\$937m	3% ▲
Non interest income	\$173m	(4%) ▼
Total income	\$1,110m	2% ▲
Operating expenses	(\$520m)	4% ▲
Underlying profit	\$590m	1% ▲
Loan impairment expense	(\$67m)	(9%) ▼
Profit before tax	\$523m	2% ▲
Income tax expense	(\$163m)	4% ▲
Cash earnings after tax	\$360m	1% ▲
Cash basic earnings per share	95.6c	(2%) ▼
Return on average tangible equity	13.8%	(60bps) ▼

# LENDING GROWTH

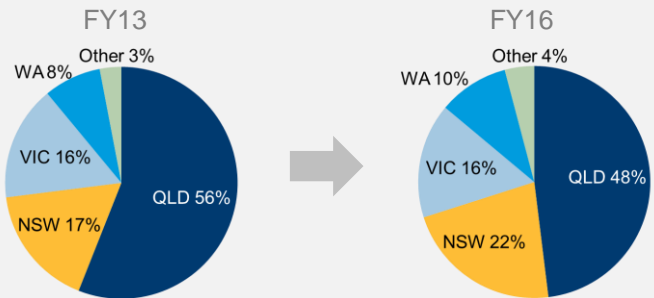
## SUMMARY

- Total lending up 5% on FY15
- Geographic mix improving – down to 48% QLD
- Strong 1H16 growth in Housing
- Prioritised margin over growth in 2H16 due to funding conditions and price competition
- Focus on growing higher margin segments in 2H16

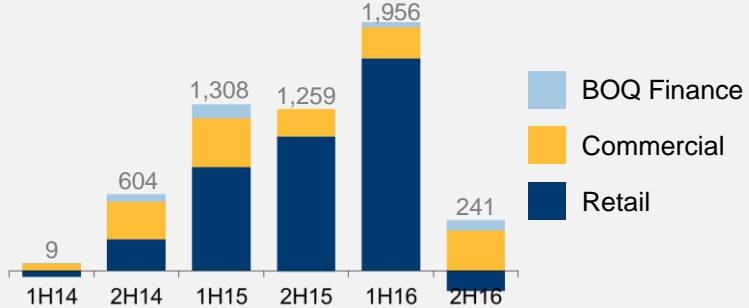
## GROSS LOANS AND ADVANCES (\$B)



## TOTAL LENDING GEOGRAPHIC MIX



## HALF YEARLY LENDING GROWTH COMPOSITION (\$M)<sup>(1)</sup>

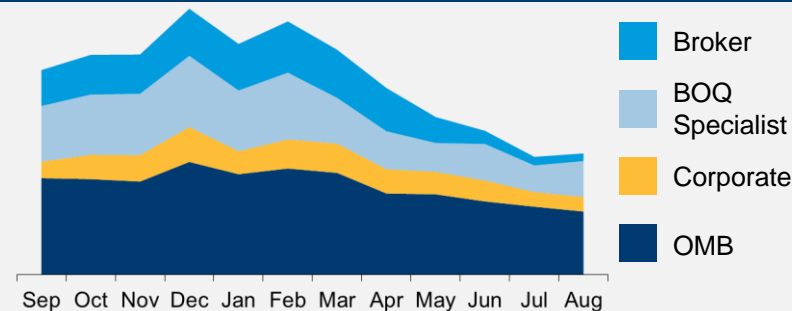


(1) Excludes Consumer lending

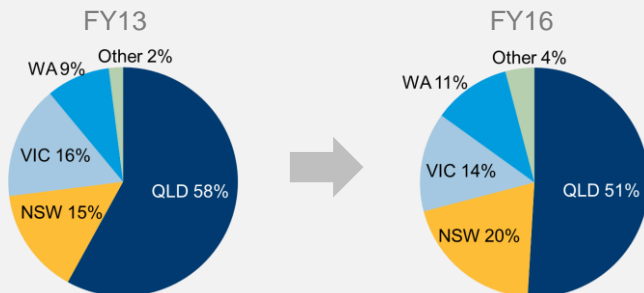
## SUMMARY

- BOQ Specialist delivered strong contribution
- Branch network remains consistent source of settlements
- Industry wide increase in refinancing activity
- Broker solid growth in 1H16 but slowed significantly in 2H16 with less competitive new business pricing

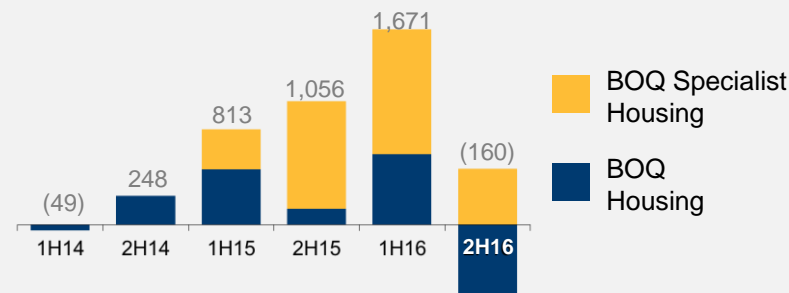
## MONTHLY HOUSING LOAN SETTLEMENTS



## HOUSING LOAN GEOGRAPHIC MIX



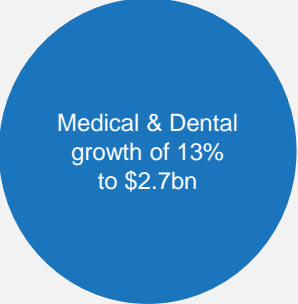
## HOUSING LOAN GROWTH (\$M)



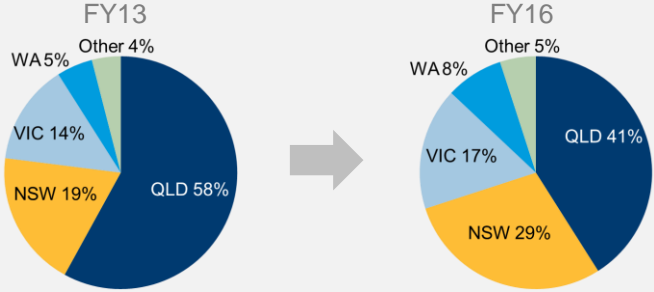
## SUMMARY

- Solid contribution from Business Banking niche segments
- BOQ Specialist & BOQ Finance performing well
- Lower quality business running off, being replaced by higher quality business

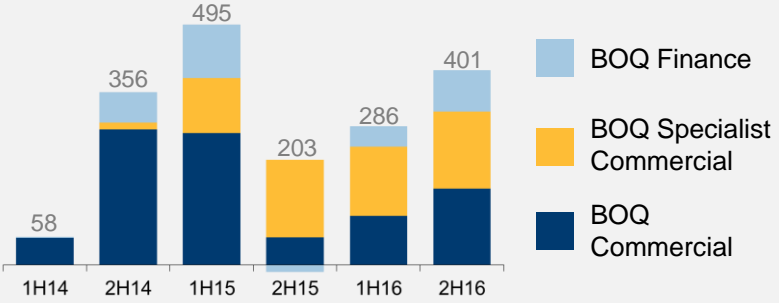
## BUSINESS BANKING NICHE SEGMENTS



## COMMERCIAL LOAN GEOGRAPHIC MIX



## COMMERCIAL LENDING & LEASING GROWTH (\$M)

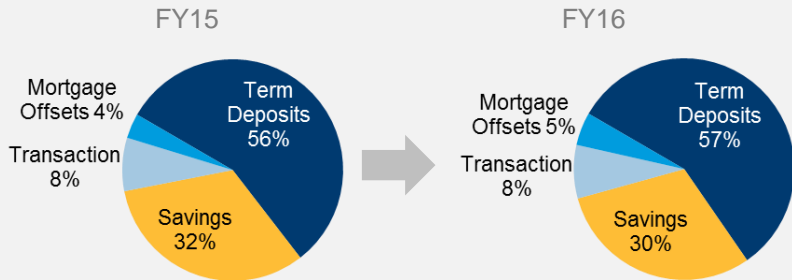




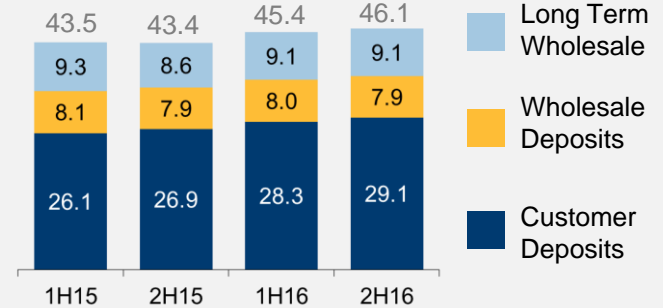
## SUMMARY

- \$2.2bn in lending growth funded by deposits with transaction account growth of \$320m
- Limited wholesale market issuance required to meet upcoming maturities
- Deposit to Loan ratio 68%

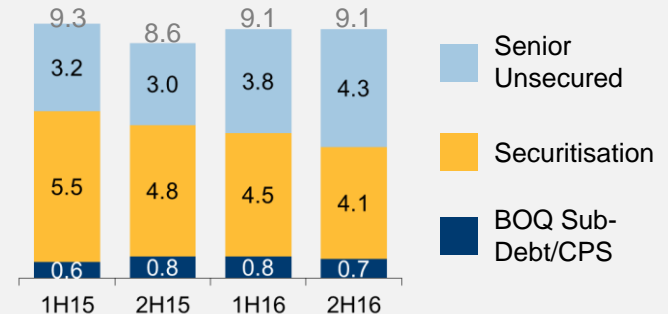
## CUSTOMER DEPOSIT MIX



## OVERALL FUNDING MIX (\$B)



## LONG TERM WHOLESALE FUNDING (\$B)

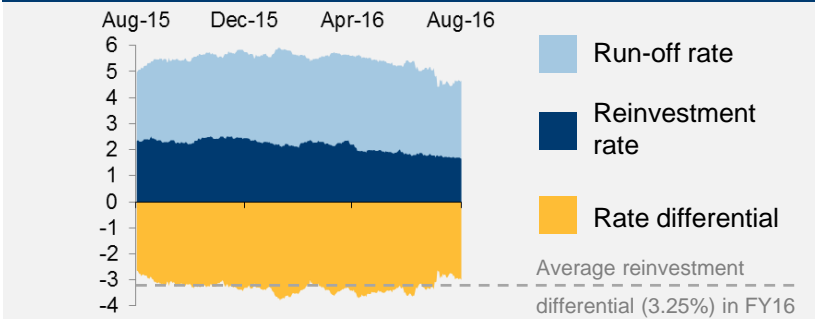


# CHALLENGING ENVIRONMENT FOR NET INTEREST MARGIN

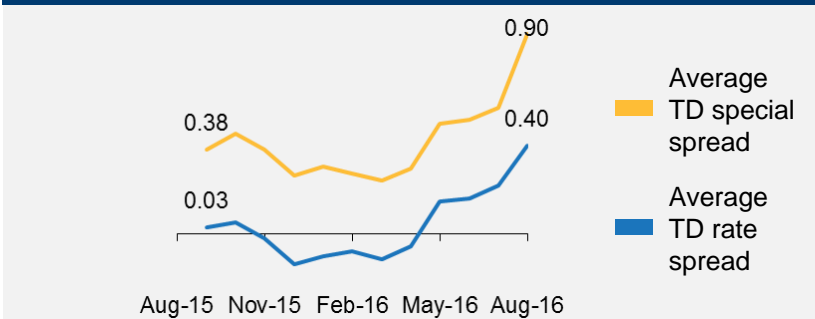
## 5YR SWAP (%): 10YEAR VIEW<sup>(1)</sup>



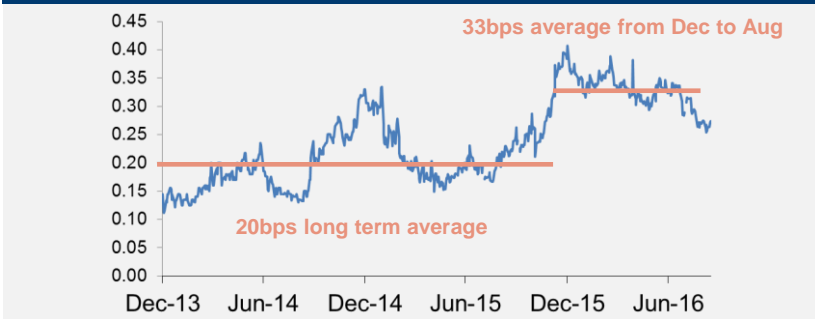
## ROLLING 5YR SWAP RATE DIFFERENTIAL (%)<sup>(1)</sup>



## INDUSTRY TERM DEPOSIT SPREADS (%)<sup>(2)</sup>



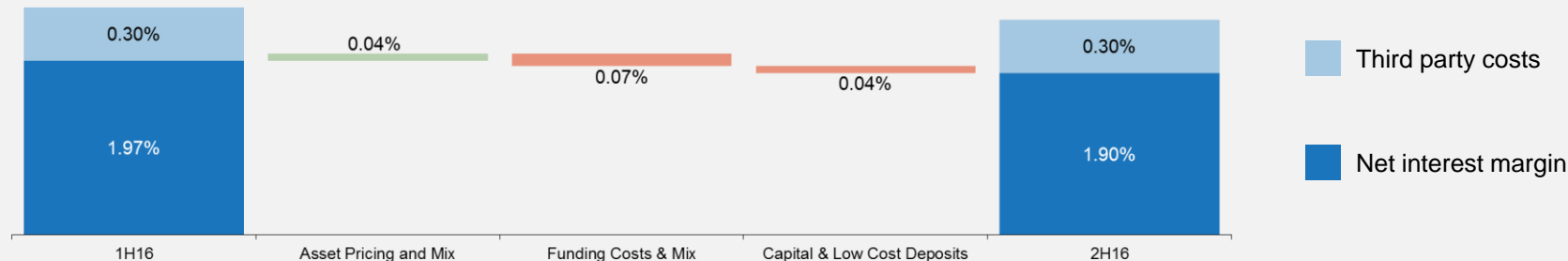
## 90-DAY BILL SPREAD TO OVERNIGHT INDEX SWAP (%)<sup>(3)</sup>



(1) Source: Bloomberg  
 (2) Spreads above 3-mth bank accepted bills, using average industry term deposit rates. Source: RBA  
 (3) Source: RBA

# MOVEMENT IN NET INTEREST MARGIN

## NET INTEREST MARGIN MOVEMENTS 1H16 TO 2H16



## 2H16 IMPACTS

- Front book vs back book housing impact ongoing
- Hedging costs have remained elevated, albeit down from peak
- Capital & Low Cost Deposits – returns on replicating portfolio impacted by lower yield curve
- Retail Term Deposit, Negotiated Term Deposit, Middle market and ST wholesale spreads have widened

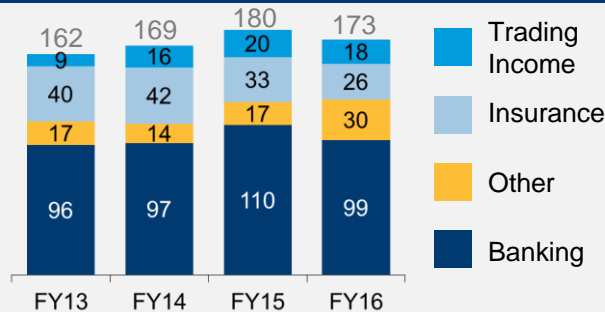
## SUMMARY OF KEY MOVING PARTS

Element	1H16	2H16	change
Asset pricing benefits	+6bps	+9bps	+3bps
Front book pricing & mix	(4bps)	(5bps)	(1bp)
Funding costs & mix	+2bps	(4bps)	(6bps)
Hedging costs	(2bps)	(3bps)	(1bp)
Capital & LCDs	(3bps)	(4bps)	(1bp)

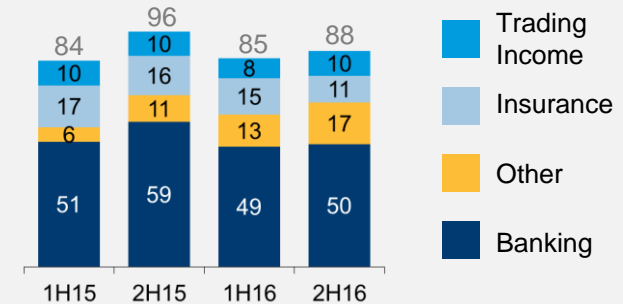
## SUMMARY

- Good performance in BOQ Finance equipment sales assisted 'Other' income
- Customer shift to lower fee products such as Clear Path mortgage product
- Change in interchange fee arrangements reduced result by \$4m
- St Andrew's Insurance transitioning to new agreement and product mix as expected; claims levels in line with expectations

### NON INTEREST INCOME BREAKDOWN (\$M): FULL YEAR



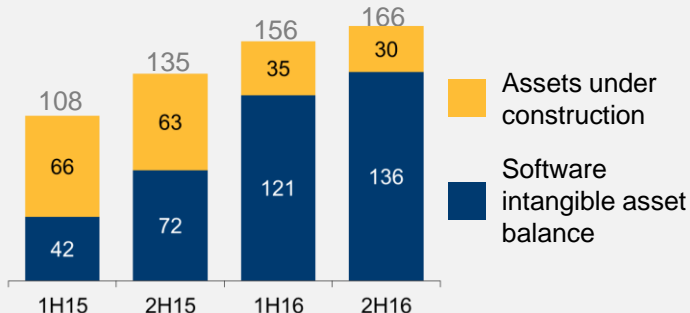
### NON INTEREST INCOME BREAKDOWN (\$M): HALF YEAR



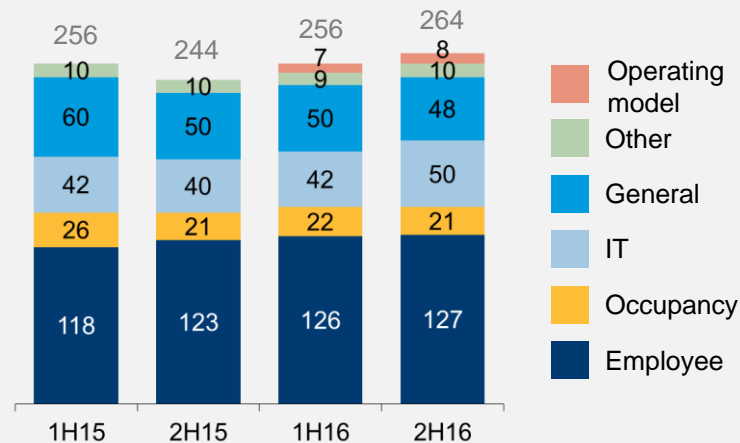
## SUMMARY

- Underlying expense growth of 4% in FY16, including planned step-up in amortisation
- Cost to Income ratio up to 46.8%; 45.5% ex one-offs
- Virgin Money mortgage roll-out added \$3m in 2H16, expected to add \$9m in FY17
- Targeting 1% underlying expense growth in FY17, including further amortisation uplift on FY16

## CARRYING VALUE OF INTANGIBLE ASSETS (\$M)



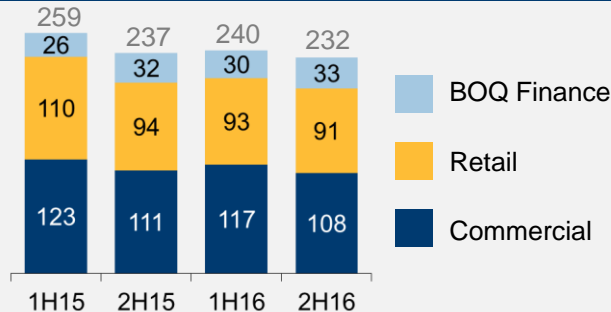
## OPERATING EXPENSE BREAKDOWN (\$M)



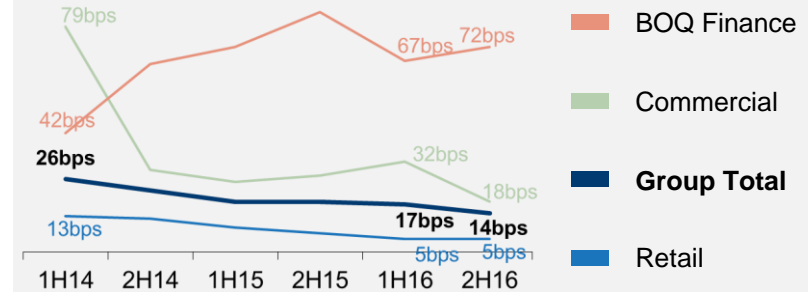
## SUMMARY

- Continued improvement in asset quality
- Commercial portfolio performance in 2H16 particularly pleasing; no new impaired assets >\$5m
- Retail portfolio benefiting from mix impact of new BOQ Specialist housing loans

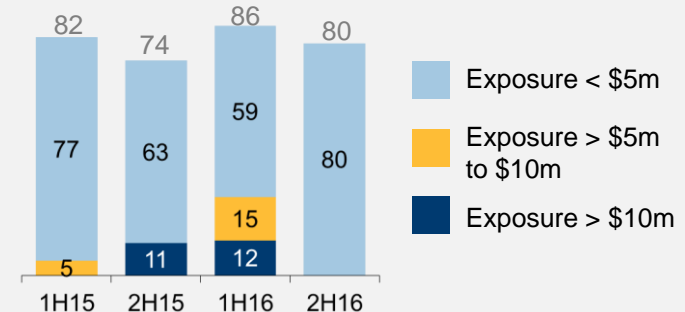
## IMPAIRED ASSETS (\$M)



## LOAN IMPAIRMENT EXPENSE BY PRODUCT (BPS)



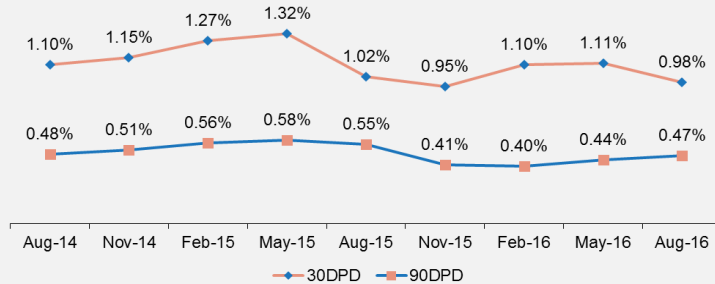
## NEW IMPAIRED ASSETS (\$M)



## SUMMARY

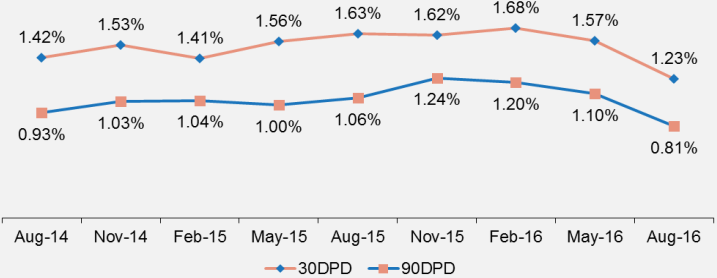
- Improving trends across all portfolios
- BOQ Specialist growth contributing to improvement
- BOQ Finance impacted by QLD & WA downturn in particular

## HOUSING ARREARS<sup>(1)(2)</sup>

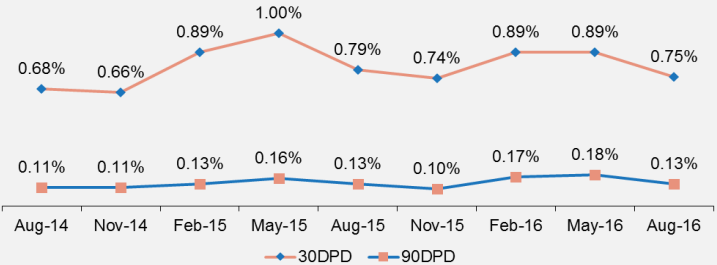


- (1) Includes BOQ Specialist  
(2) Housing excluding Lines of Credit

## COMMERCIAL ARREARS<sup>(1)</sup>



## BOQ FINANCE ARREARS

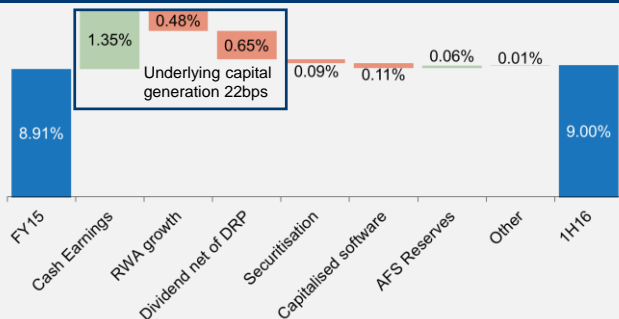


# STRONG CAPITAL POSITION MAINTAINED

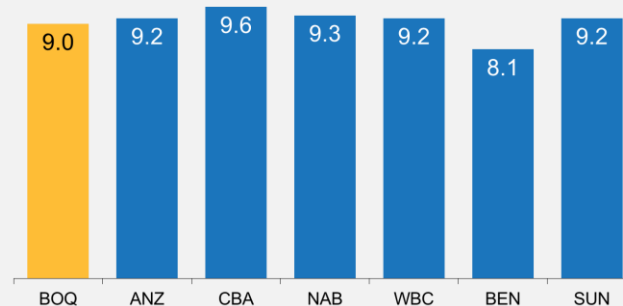
## SUMMARY

- Capital position compares well against peers, particularly given BOQ's more conservative risk weightings
- Basel 4 should level the playing field further; Potential upside in SME risk weights
- Good progress made towards advanced accreditation if size of the prize warrants accelerating that step

## COMMON EQUITY TIER 1 RATIO MOVEMENTS



## PEER CET1 COMPARISON<sup>(1)</sup>



## OPPORTUNITIES FROM BASEL 4

Lower risk weights for SME & Leasing books

Increases BOQ's CET1 ratio and improves returns on SME lending

Capital floor for advanced banks

>70% capital floor would help close the gap between advanced & standardised

(1) Based on most recent Pro-forma CET1 figures published by peers



# PROGRESS TOWARDS ADVANCED ACCREDITATION

## Initiatives in place

Credit risk	Credit policy framework Credit models Collective Provision/GRCL Lending origination systems
Operational risk	Operating model & framework Governance framework implementation Incident management system
Market risk	Asset Liability Management (ALM) System Policy review & governance framework Integration of Funds Transfer Pricing (FTP) into ALM
Enterprise management	Risk appetite statements Compliance gateways & Risk KPIs

Application for Advanced



# SUMMARY & OUTLOOK

JON SUTTON

Managing Director & CEO



## Economic

- Low interest rates and low unemployment supporting economic growth
- QLD benefiting from tourism
- Mining investment downturn impacting some regions

## Industry

- Lower credit growth
- ROE impacted by lower for longer interest rates
- Conduct and culture focus
- Rapidly changing customer expectations

## Regulatory

- Revised standardised approach
- Capital floor for advanced banks
- Staged approach to advanced accreditation
- Net Stable Funding Ratio

Vision ...

Our dream is to create AUSTRALIA'S MOST LOVED BANK

Strategy ...

**Focus on niche segments that value a more intimate customer relationship**

FY17 priorities ...

Customer in charge	Grow the right way	There's always a better way	Loved like no other
<ol style="list-style-type: none"> <li>Expansion of mortgage aggregators for Virgin Money</li> <li>Enhance digital customer experience</li> <li>Ongoing branch network optimisation</li> </ol>	<ol style="list-style-type: none"> <li>Optimise deposit pricing using data analytics</li> <li>Develop specialist niche capability in franchising and hospitality</li> <li>Focus investment in high margin businesses</li> </ol>	<ol style="list-style-type: none"> <li>Complete roll out of new origination &amp; leasing systems</li> <li>Deliver return on investment in efficiency programs</li> <li>Implement centralised mortgage hub</li> </ol>	<ol style="list-style-type: none"> <li>Invest in leadership and talent</li> <li>Build gender diversity towards 50% in senior management by 2020</li> <li>Complete ethics training roll-out</li> </ol>

Outcomes ...

**Outperform sector EPS growth**

- 1 Subdued revenue growth across the industry to persist
- 2 Focus on growing in high margin segments
- 3 Maintain risk discipline
- 4 Deliver additional efficiency program benefits
- 5 Continue with execution of strategy



# BOQ

## FY16 RESULTS PRESENTATION

### 6 OCTOBER 2016

FOR THE YEAR ENDED 31 AUGUST 2016





# APPENDICES



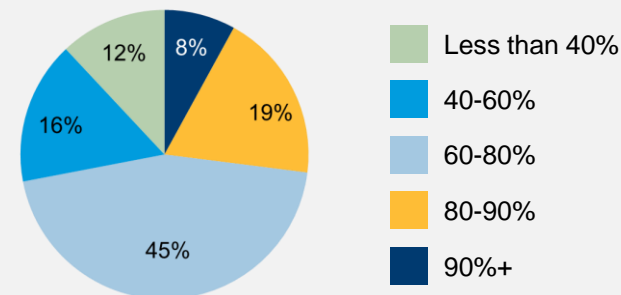
## SUMMARY

- Quality continues to improve under revised risk appetite
- Higher proportion of fixed rate lending in FY16
- Line of credit portfolio continues to reduce

## PORTFOLIO METRICS

Metrics (%)	2H15	1H16	2H16
Owner occupied	58	57	58
Investment	42	43	42
Broker originated	6	7	8
Weighted avg LVR	65	62	63
Line of Credit	11	10	9
Avg loan balance	\$258k	\$258k	\$262k
Variable rate	81	77	75
Fixed rate	19	23	25

## HOUSING PORTFOLIO LVR BANDS



## SETTLEMENT METRICS

Metrics (%)	2H15	1H16	2H16
Owner occupied	63	56	59
Investment	37	44	41
Broker originated	14	19	15
Weighted avg LVR	68	68	67
Line of Credit	4	3	3
Avg loan balance	\$354k	\$356k	\$376k
Variable rate	75	56	69
Fixed rate	25	41	31



# MINIMAL EXPOSURE TO HIGH RISK SECTORS

## Apartment construction exposures<sup>(1)</sup>

- \$215m current exposure to residential construction
- 30 developments across 3 states, majority completing 2016 through 2017
- Highest concentration in VIC and NSW, well diversified intra-state

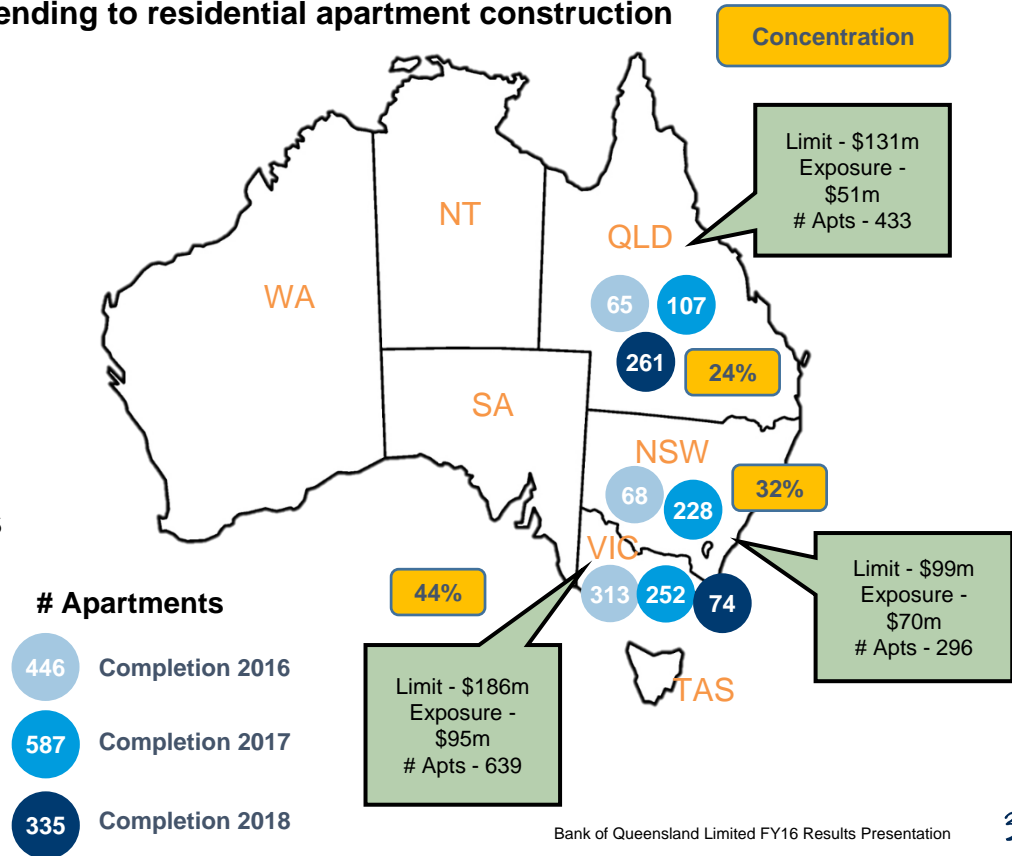
## Regional Housing exposures

- No material regional housing exposures

## Regional Commercial & Leasing exposures

- No systemic issues emerging
- Direct mining industry exposure ~\$110m

## Lending to residential apartment construction



(1) Projects over \$5m. Data as at 30 September 2016

# ABBREVIATIONS

1H: First half of financial year  
2H: Second half of financial year  
30DPD: 30 days past due  
90DPD: 90 days past due  
AFS: Available for sale  
ALM: Asset & Liability Management  
APRA: Australian Prudential Regulation Authority  
Apts: Apartments  
Avg: Average  
BDD: Bad & Doubtful Debt Expense  
bps: basis points  
CET1: Common Equity Tier 1  
cps: Cents per share  
CPS: Convertible Preference Shares  
CTI: Cost-to-income ratio  
DRP: Dividend Reinvestment Plan  
EPS: Earnings per share

FTP: Funds transfer pricing  
FY: Financial year  
GLA: Gross Loans & Advances  
GRCL: General Reserve for Credit Losses  
KPI: Key performance indicator  
LCD: Low cost deposit  
LOC: Line of Credit  
LVR: Loan to valuation ratio  
NIM: Net Interest Margin  
OMB: Owner Managed Branch  
RBA: Reserve Bank of Australia  
ROE: Return on equity  
ROTE: Return on tangible equity  
RWA: Risk weighted assets  
SME: Small and Medium Enterprises  
TD: Term deposit  
VMA: Virgin Money Australia

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